Inter-City Gas
LIMITED

ANNUAL REPORT

NINETEEN HUNDRED AND SEVENTY-SIX

TO THE SHAREHOLDERS:

Net income for the six months to June 30, 1976 totalled $1.7 million, up 24% over the same period last year. Earnings per common share amounted to 37c compared with 30c for the first half of 1975.

Operating revenues to date total $31.3 million, a gain of 31% from last year. This increase is attributed to higher sales of natural gas with the passing on of increased costs of gas purchased, together with significant increases in revenues and profits of its exploration and equipment divisions.

On August 4, 1976, the Company finalized the purchase of all the shares of Elwill Development Limited for $34.8 million. Elwill's major assets are 2,550,256 common shares and $5.9 million second preference shares of Canadian Hydrocarbons Limited. Inter-City's effective interest in the common shares of Canadian Hydrocarbons now stands at 49.8%.

Both Inter-City and Canadian Hydrocarbons are primarily engaged in the exploration, development and distribution of hydrocarbon fuels (natural gas, propane and gasoline) and related products, equipment and services. We intend to ultimately combine the operations of Inter-City and Canadian Hydrocarbons by the most practical means of corporate combination appropriate at such time. This combination will result in a strong organization well equipped to handle the energy needs of a diversified market.

R. G. GRAHAM
President

August 16, 1976

TRANSMISSION AND
DISTRIBUTION OF NATURAL GAS

MANUFACTURING AND
DISTRIBUTION OF HEATING EQUIPMENT

EXPLORATION AND DEVELOPMENT
OF OIL AND GAS RESOURCES

Inter-City Gas
LIMITED

Inter-City Gas

QUARTERLY REPORT
FOR THE SIX MONTHS ENDED JUNE 30, 1976

INTER-CITY GAS LIMITED
AND SUBSIDIARY COMPANIES

Consolidated Statement of Income (Unaudited)
For the Six Months Ended June 30, 1976

	1976	1975
OPERATING REVENUE		
Sale of natural gas		
Utility Operations	$21,237,032	$17,208,610
Exploration Operations	2,598,222	1,249,994
Sale of Manufactured Goods	7,301,952	5,333,042
Other Revenue	208,623	156,738
	31,345,829	23,948,384
OPERATING EXPENSES		
Natural Gas Purchased	16,192,923	11,791,837
Cost of Manufactured Goods Sold	5,732,466	4,246,866
Operating and Maintenance	3,459,671	2,798,360
Municipal Taxes	608,352	606,068
Depreciation and Depletion	976,087	792,726
	26,969,499	20,235,857
OPERATING PROFIT	4,376,330	3,712,527
FINANCIAL EXPENSES		
Interest on Long-Term Debt	1,136,612	1,041,733
Other Interest	625,551	468,770
Amortization of Financing Expenses	36,874	50,926
Interest Capitalized	(366,696)	(265,885)
	1,432,341	1,295,544
	2,943,989	2,416,983
PROVISION FOR INCOME TAXES	1,231,000	1,040,000
CONSOLIDATED NET INCOME FOR THE SIX MONTHS	$ 1,712,989	$ 1,376,983
NET INCOME PER COMMON SHARE	$ .37	$ .30
AVERAGE COMMON SHARES OUTSTANDING	3,722,524	3,422,620

INTER-CITY GAS LIMITED
AND SUBSIDIARY COMPANIES

Consolidated Statement of Changes in Financial Position (Unaudited)
For the Six Months Ended June 30, 1976

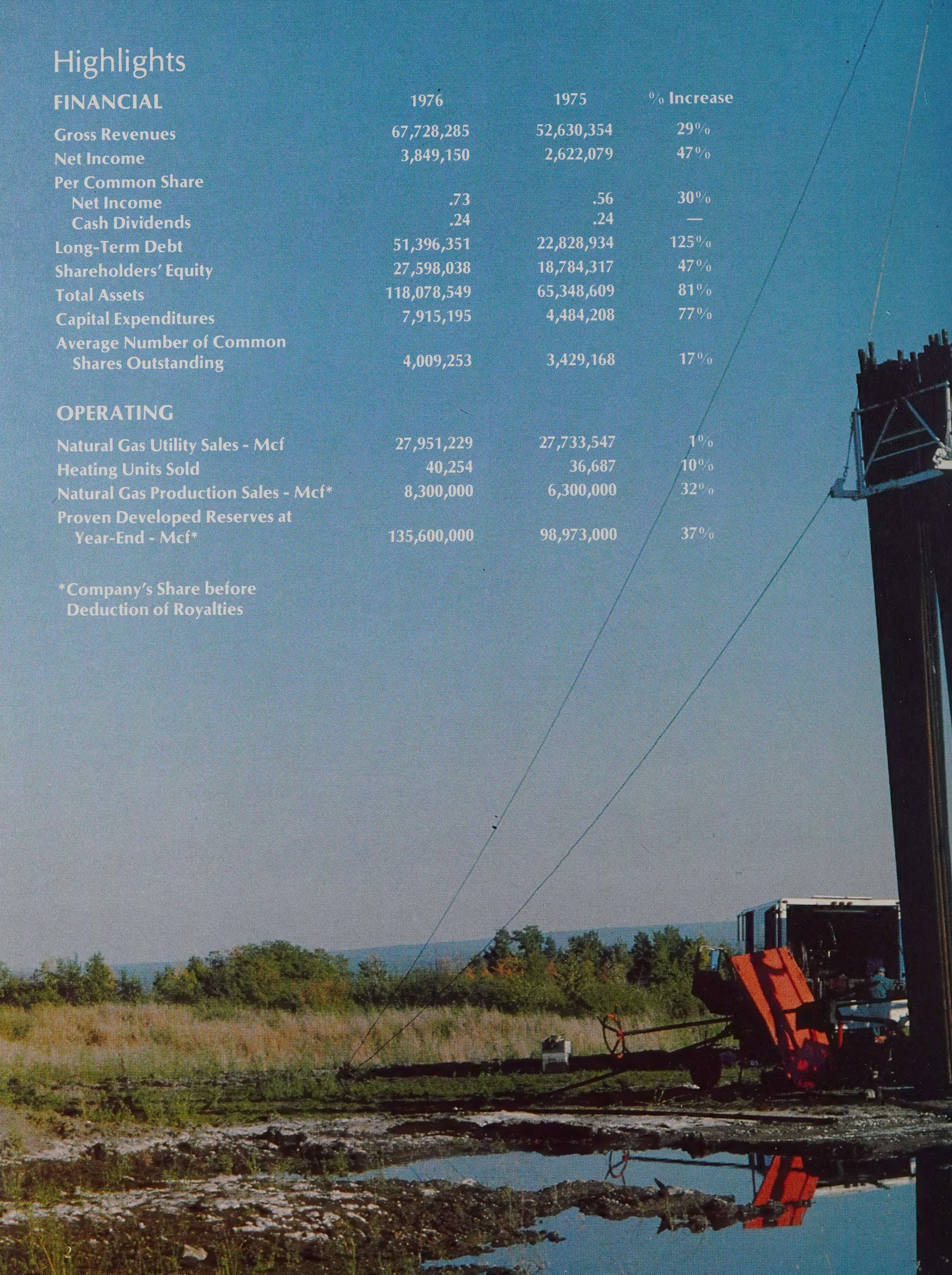
	1976	1975
SOURCE OF FUNDS		
Provided from Operations	$ 3,376,848	$ 2,969,340
Proceeds from Issue of Common Shares	3,006,735	–
Proceeds from Term Loan	–	4,500,000
Decrease in Investments	–	31,182
	6,383,583	7,500,522
USE OF FUNDS		
Additions to Utility System and Other Equipment	269,520	914,796
Additions to Petroleum and Natural Gas Properties, Exploration Costs and Well Equipment	2,515,056	493,675
Repayment of Long-Term Debt	1,626,201	2,039,260
Redemption of Preference Shares	104,000	23,600
Dividends Paid to Shareholders	867,566	770,602
Financing Expenses, Rate Hearings and Other Deferred Charges	281,933	103,647
Refund of Customers' Contributions in Aid of Construction	12,838	871
Purchase of Shares of Subsidiary Company	–	255,770
Increase in Investments	119,860	–
	5,796,974	4,602,221
INCREASE IN WORKING CAPITAL	$ 586,609	$ 2,898,301

Contents

Annual Shareholders' Meeting

The Annual General Meeting of Shareholders will be held at the Winnipeg Inn, Winnipeg, Manitoba, at 2:00 p.m., May 13, 1977.

Inter-City Gas Limited

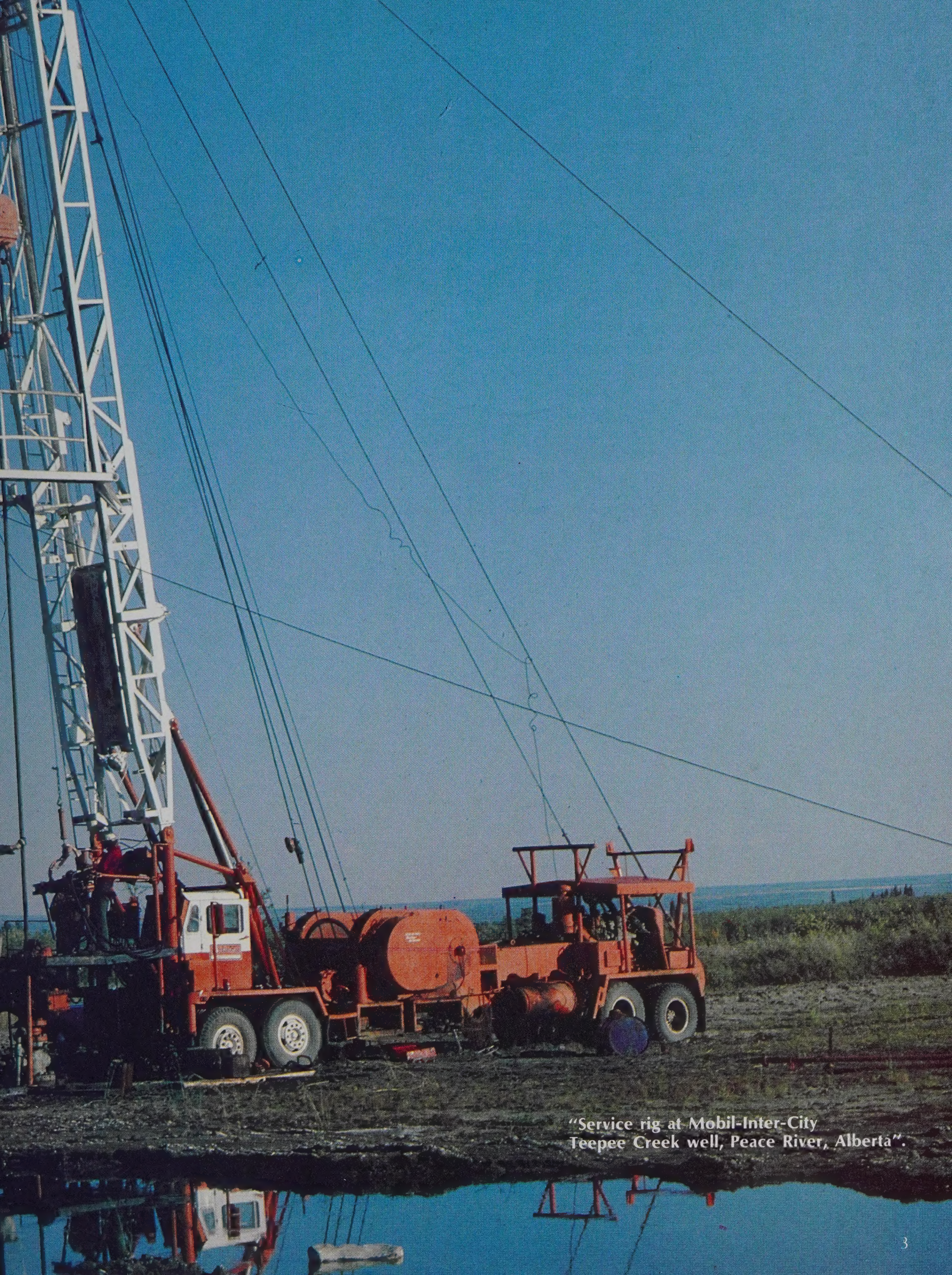


Highlights

FINANCIAL	1976	1975	% Increase
Gross Revenues	67,728,285	52,630,354	29%
Net Income	3,849,150	2,622,079	47%
Per Common Share			
Net Income	.73	.56	30%
Cash Dividends	.24	.24	—
Long-Term Debt	51,396,351	22,828,934	125%
Shareholders' Equity	27,598,038	18,784,317	47%
Total Assets	118,078,549	65,348,609	81%
Capital Expenditures	7,915,195	4,484,208	77%
Average Number of Common Shares Outstanding	4,009,253	3,429,168	17%

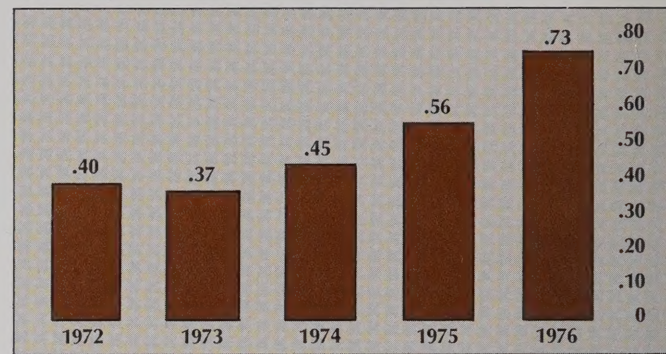
OPERATING			
Natural Gas Utility Sales - Mcf	27,951,229	27,733,547	1%
Heating Units Sold	40,254	36,687	10%
Natural Gas Production Sales - Mcf*	8,300,000	6,300,000	32%
Proven Developed Reserves at Year-End - Mcf*	135,600,000	98,973,000	37%

*Company's Share before Deduction of Royalties

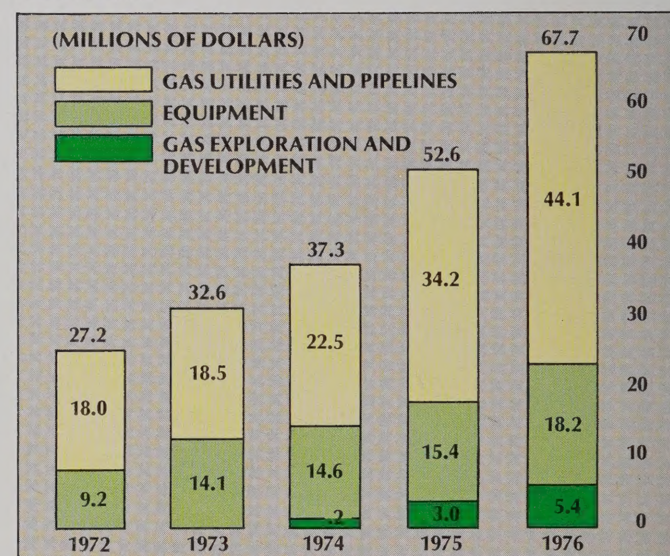


"Service rig at Mobil-Inter-City Teepee Creek well, Peace River, Alberta".

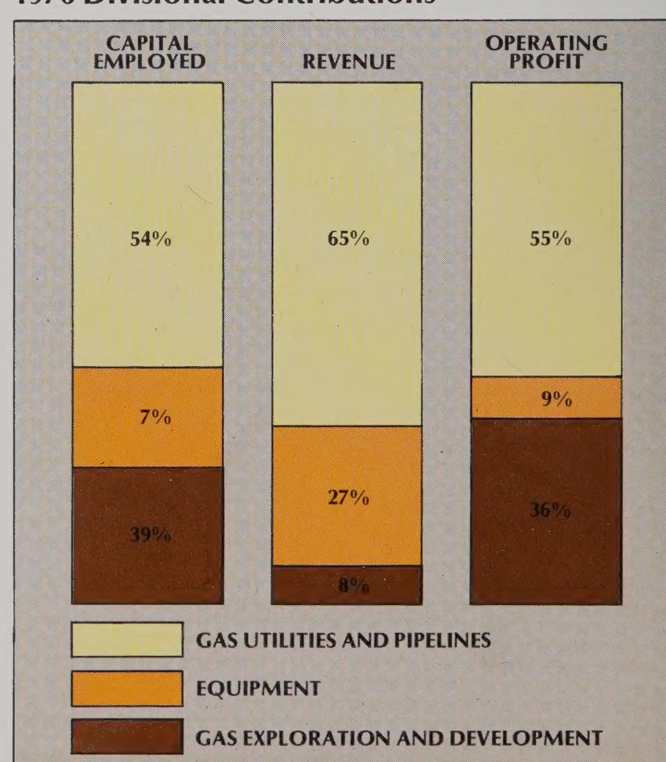
Earnings Per Share



Revenues



1976 Divisional Contributions



Report to Shareholders

R.G. GRAHAM
President

1976 was both a successful and eventful year for your Company. Net income increased 47% and earnings per common share increased 30% to 73¢ per share from 56¢ last year. The rights offering to shareholders in April, 1976, resulted in the issue of 859,000 common shares and increased the average number of common shares outstanding during the year by 17% to 4,009,000 shares outstanding. Dividends were paid at the rate of 24¢ per common share.

Total revenues increased by 29% to $67,728,000 from $52,630,000. With relatively consistent operating profits contributed by both the utility and equipment operations in 1976, as compared with 1975, the increase in earnings this year is attributed to higher natural gas production and to our investment in Canadian Hydrocarbons Limited.

The highlight of the year was the acquisition, in August, 1976, of 49.8% of the common shares of Canadian Hydrocarbons Limited. It is our wish to ultimately combine the operations of Canadian Hydrocarbons and Inter-City into an organization which will be able to serve the diversified energy needs of a broad market. We believe that the shareholders, the employees, and the customers of Canadian Hydrocarbons and Inter-City will be served by a stronger, more dynamic organization through such a combination. It is contemplated that a plan of full corporate combination, by the most practical means then appropriate, will be announced in the near future. Details of the acquisition are commented on later in this report.

Inter-City and Canadian Hydrocarbons are engaged in several compatible facets of the energy industry. Each has gas utility operations of approximately the same size measured in terms of revenues and profits. Inter-City serves areas in Manitoba, Ontario and Northern Minnesota; Canadian Hydrocarbons (through subsidiaries) serves areas in Alberta, British Columbia and Manitoba. Inter-City operates a growing gas and oil exploration division while Canadian Hydrocarbons participates in exploration through its effective ownership of 45.2% of Canadian Homestead Oils Limited. Canadian Hydrocarbons is Canada's largest distributor of propane fuel; Inter-City has the largest share of the Canadian market for furnaces utilizing gas, propane, oil and electricity.

In addition to the $34,254,000 investment in Canadian Hydrocarbons Limited, capital expenditures in 1976 totalled $7,915,000 compared to $4,484,000 in 1975. This increase is primarily due to the construction and development of natural gas production plants and gathering systems. Total assets at December 31, 1976 amounted to $118,079,000, compared with $65,349,000 a year ago.

During the year the Company raised $3,008,000 by a new issue of common shares, $4,000,000 by an issue of 200,000 10½% Series C first preference shares, and $36,000,000 by term bank loans with maturity dates varying between 1978 and 1983.

It is your Company's intention to continue the emphasis upon development within the energy distribution industry and to pursue expansion of both product lines and geographic markets.

Submitted on behalf of the Board of Directors.

President and Chief
Executive Officer
Winnipeg, Manitoba
April 7, 1977

Investment in Canadian Hydrocarbons Limited

In August, 1976, Inter-City Gas Limited purchased all the issued shares of Elwill Development Limited for $34,254,000 in cash, including financing costs. Elwill's major assets were 2,550,256 common shares, $5,915,000 par value second preferred shares of Canadian Hydrocarbons Limited and $1,900,000 in working capital. Elwill had notes payable of $5,800,000.

Subsequently, the Company purchased an additional 6,400 common shares of Canadian Hydrocarbons, bringing our effective interest to 49.8%.

Canadian Hydrocarbons, along with its subsidiary companies is engaged in:

— refining and marketing of petroleum products in Canada and five north-western states of the U.S.A.;
— operation of gas utilities in Manitoba, Alberta and British Columbia and the electric utility in Yellowknife, N.W.T.;
— exploration for and development of oil and natural gas in Canada and the U.S.A.;
— steel pipe fabrication;
— production and distribution of forest products.

Canadian Hydrocarbons own 45.2% of the outstanding common shares of Canadian Homestead Oils Limited.

In 1976, Canadian Hydrocarbons reported net income of $5,341,000 on total revenues of $329,466,000.

Inter-City's equity share of this income, after providing for carrying costs of the investment, contributed approximately $240,000 or 6¢ per share to Inter-City's 1976 net earnings.

Gas regulation station and major industrial customer.

Gas Utilities and Pipelines

Sales of natural gas by the utility and pipeline division totalled $43,415,000, an increase of $9,383,000 over 1975. This 28% rise in revenue primarily reflects the pass through to our customers of increases in the cost of gas. Although gross profits did increase over last year by 5%, operating profits for the division dropped 8% to $4,997,000. This decrease was mainly attributable to the decline in the value of the Canadian dollar during 1976.

The Minnesota operating area experienced periodic curtailment of the volumes of gas historically available for sale to industrial customers. The Company recognized the probability of this industrial curtailment several years ago and since 1974 has directed its marketing efforts towards shifting gas volumes from industrial customers to residential and commercial consumers. Our supply of gas for Minnesota under contract demand remains unchanged and is available for service to additional residential consumers. The supply of natural gas for our Canadian utility operations is provided under long-term contract sufficient to meet the foreseeable requirements of both present and future customers.

At the year end, utility customers totalled 29,781, an increase of 1,082 customers from one year ago. The division services 67 communities in Manitoba, Ontario and Minnesota. Total volume of natural gas sold by the utility and pipeline operation was 27,951,000 mcf, up slightly from last year.

Development of a customer service program in 1976 supplemented revenues and profits of the Minnesota operation. This program was well received by our customers and will be extended into other operating areas.

Installation of gathering system, Many Islands area, Alberta.

Utility staff on work site.

Utility staff tapping pipeline to service new customer.

Equipment

The equipment division manufactures residential and commercial heating products at factories located in Winnipeg and St. Catharines. Most of these products, as well as related products manufactured by others, are distributed to the heating trade by wholly-owned branch supply houses at locations from Ontario to British Columbia. Approximately 15 to 20 percent of our manufactured products are sold on a direct factory account basis to distributors in areas which are not serviced by our equipment supply branches, or on a brand line basis to major national accounts.

Revenue from the division increased by 20% over 1975. We sold approximately 9% more units of our own manufactured products in 1976 than in 1975. Our share of the Canadian market for residential heating equipment was essentially the same during 1976 as in 1975, with approximately 23% of the gas furnaces, 33% of the electric furnaces and 9% of the oil furnaces sold in Canada.

Operating profit for the division was $840,000 compared to $930,000 in 1975. The drop is largely due to problems in producing a new multi-fuel unit. Required modifications to this new unit were significant and costly and did not appear until the unit had entered the manufacturing phase. However, the problems appear to have been overcome and a good market seems to be available for this product during 1977.

We have also arranged for distribution of additional commercial products which should serve to improve profits for 1977.

Products merchandised by Intercity Energy Supply Division.

Testing laboratory, St. Catharines, Ontario.

Furnace assembly line — Winnipeg.

Gas Exploration & Development

Revenue from natural gas production during 1976 was $5,579,000, an increase of 94% over 1975 with a corresponding increase in contribution to operating profit. Average daily natural gas production, net of royalties, was 14,530 mcf.

At December 31, 1976, an independent engineering consulting firm assigned the following reserves to properties held by the Company:

BEFORE ROYALTY	**Proven**	**Probable**	**Combined**
Natural gas (billions of cubic feet)	135.6	32.2	167.8
Natural gas liquids (thousands of bbls.)	45.2	23.3	68.5
Oil (thousands of bbls.)	16.8		16.8
AFTER ROYALTY	**Proven**	**Probable**	**Combined**
Natural gas (billions of cubic feet)	84.6	19.6	104.2
Natural gas liquids (thousands of bbls.)	33.5	16.9	50.4
Oil (thousands of bbls.)	14.7		14.7

After royalty volumes are calculated as those that would remain were all future royalty payments taken as a share of producible reserves.

During 1976, the Company acquired exploratory lands in the Handhills, Flat Lake, Atmore, Sarrail, Tweedie, Amigo, Fox Creek and Sterco areas of Alberta. These properties cover a wide range of production opportunities from shallow gas in east-central Alberta to deep stratigraphic prospects in west-central and northwest areas. These acquisitions totalled 42,560 gross acres, bringing Inter-City's interest in petroleum and natural gas lands to 551,070 acres of which 155,777 acres are net to the Company.

During the year the Company participated in the drilling of 100 wells of which 80 were development wells and 20 were exploratory - 90 of these wells are productive.

Development drilling was concentrated primarily in these major areas; Tweedie, Many Islands Lake and Hilda.

Drilling operation, Lac La Biche area, Alberta.

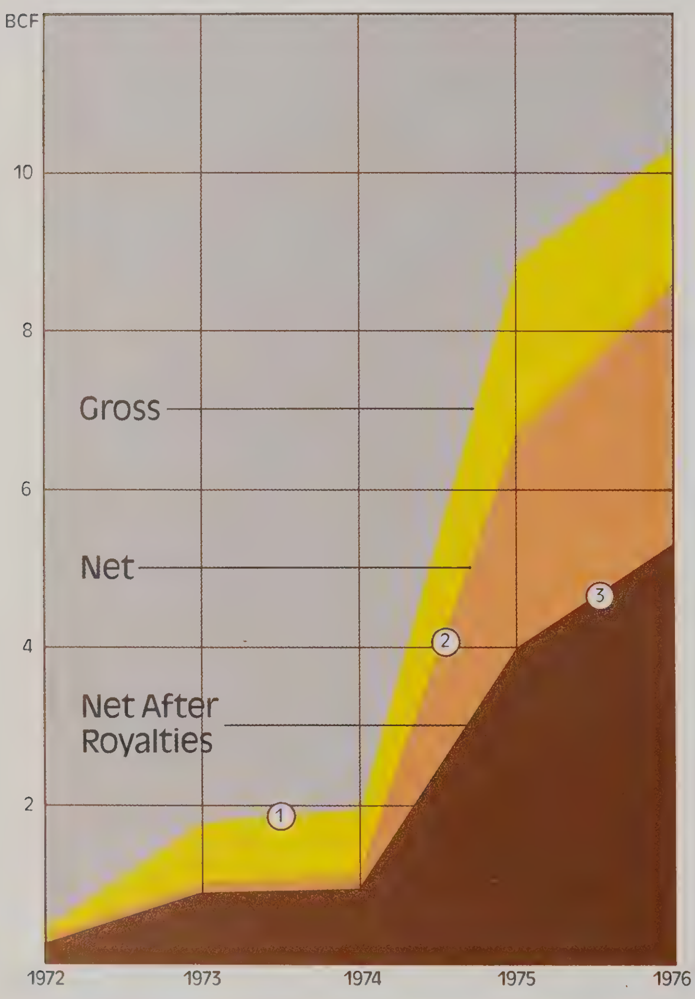
Drilling crew on site.

Initial development of the Tweedie gas field was completed late in the year and delivery commenced on December 14, 1976, at a daily rate of 14,000 mcf. The Company's share of this production, after other interests and crown royalties is approximately 40%.

Although infill drilling to optimize delivery of the Milk River formation underlying our Many Islands Lake property was concluded in 1976, this development program resulted in the discovery of gas in formations both above and below the primary objective. As a result, 18 dual zone wells were completed during the year and plans are now formulated for further development of these additional reserves.

Drilling in the Hilda field was concluded during 1976 together with the installation of gathering and compression facilities sufficient to deliver approximately 5,000 mcf per day. The Company is operator and 50% working interest partner in the Hilda field.

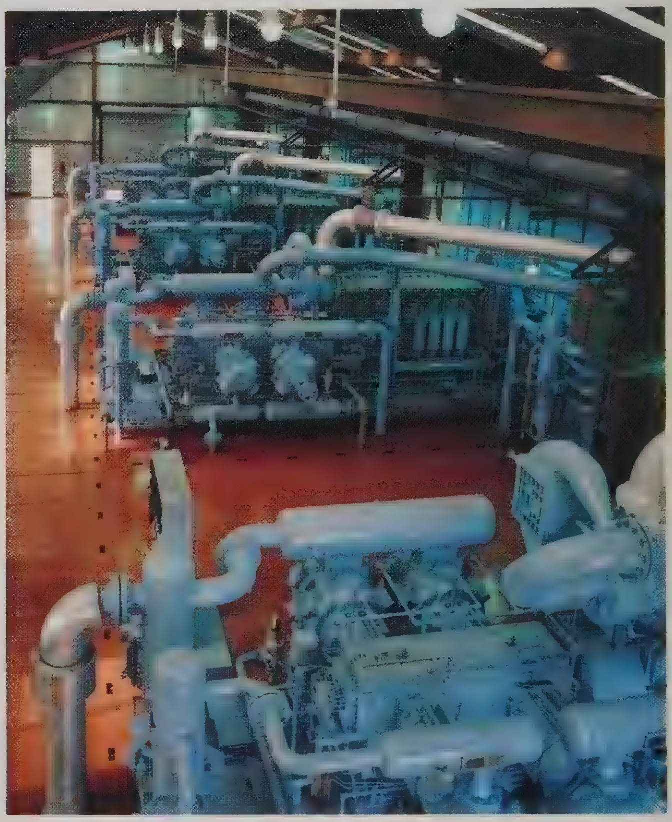
The 3-year exploration program, in which Inter-City and partners participate with Mobil Oil of Canada, will conclude in July, 1977. To December 31, 1976, 19 wells in 9 prospect areas in the deep basin and foothills area of Alberta had been completed, including 6 development wells. Three of these wells are currently producing natural gas and 10 are capable of production at such time as transmission pipeline facilities are extended to the areas.



Inter-City Gas Limited annual gas production (billions of cubic feet).

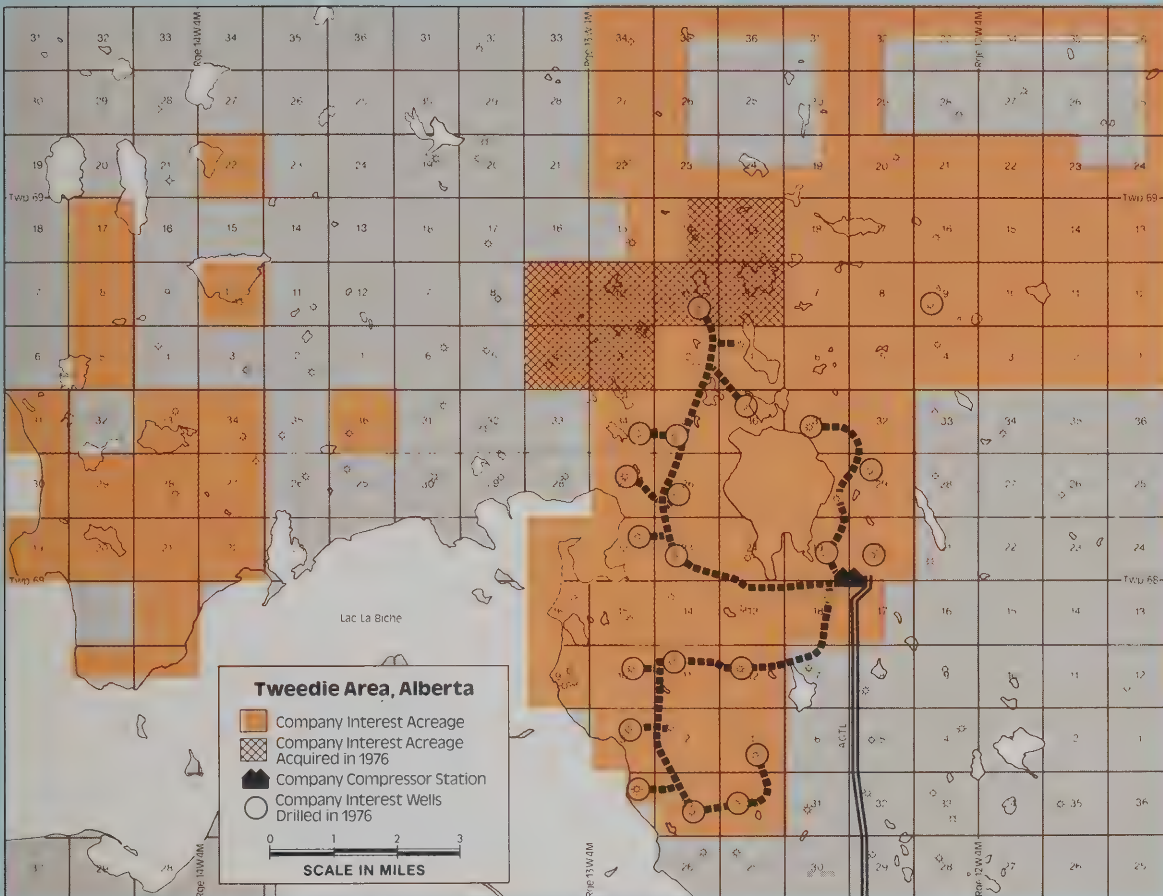
1. **Total gas produced from Inter-City operated properties and Inter-City net gas before royalty from non-operated properties.**
2. **Inter-City net production before royalties from all properties.**
3. **Inter-City net production after royalties from all properties.**

Compressor station, Many Islands Lake area, Alberta.

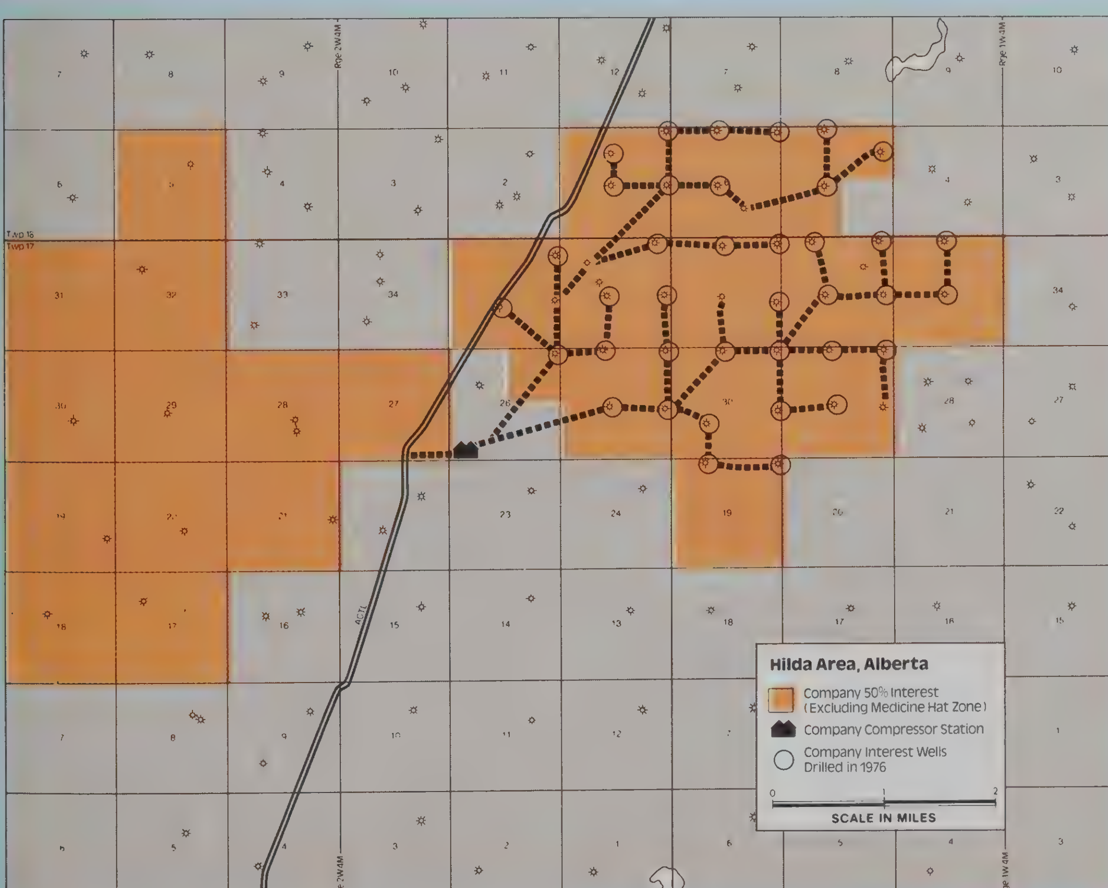



Amigo
Hotchkiss
Springburn
Teepee Creek
Tweedie
Atmore
Sarrail
Hope Lake
Fox Creek West
Baseline Lake
Nose Hill Creek
Rosevear
Edmonton
Sterco
Chedderville
Bearberry
Twining
Sullivan Lake
Rowley
Garden Plains
Sounding Creek
Hand Hills
Calgary
Hilda
Many Islands
Medicine Hat
Medicine Hat South
Walsh
Production and Development
Exploration

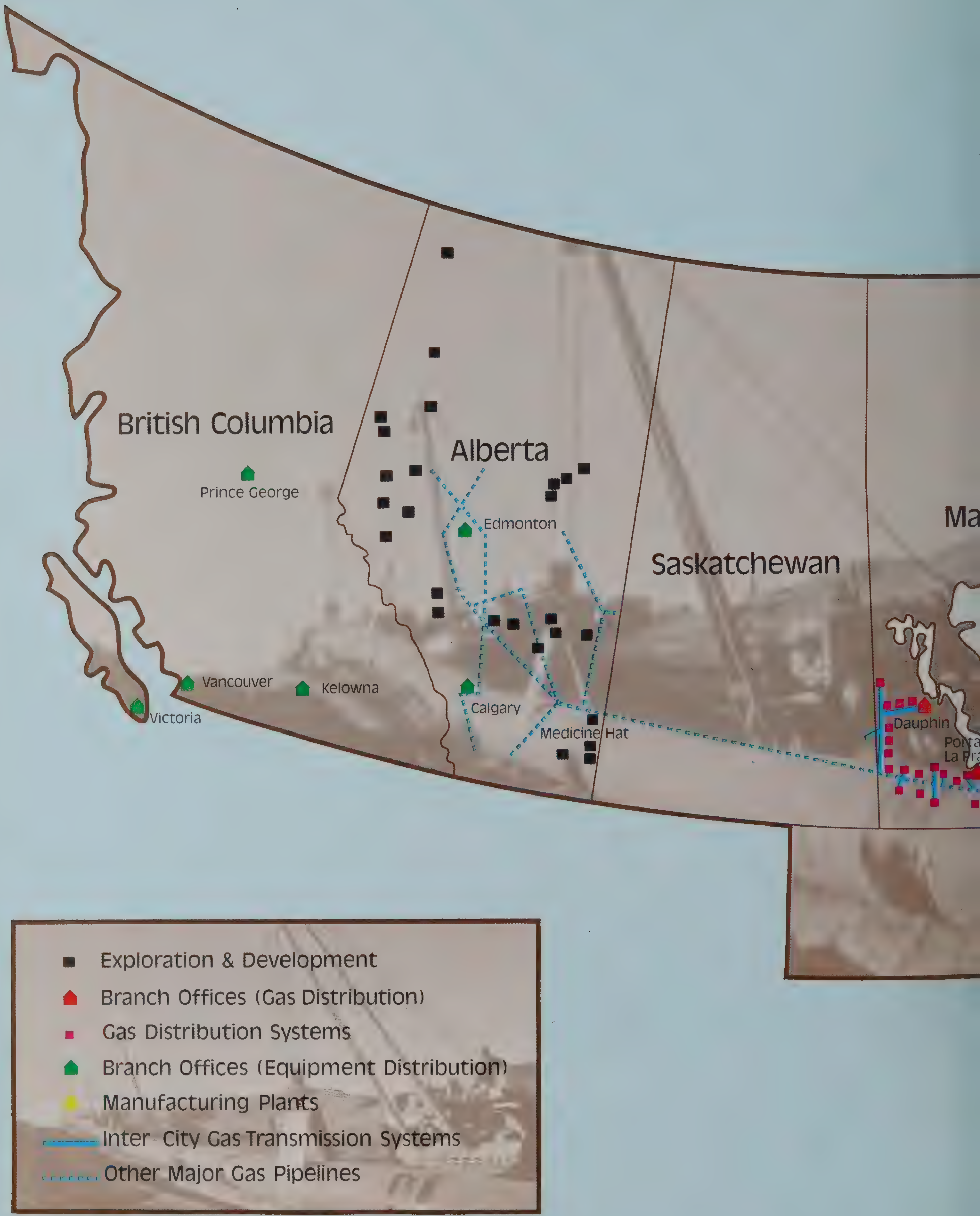

Many Islands Area, Alberta
Company Interest Acreage
Company Compressor Station
Company Interest Wells Drilled in 1976
SCALE IN MILES
AGTL



Tweedie Area, Alberta
Company Interest Acreage
Company Interest Acreage Acquired in 1976
Company Compressor Station
Company Interest Wells Drilled in 1976
SCALE IN MILES
Lac La Biche

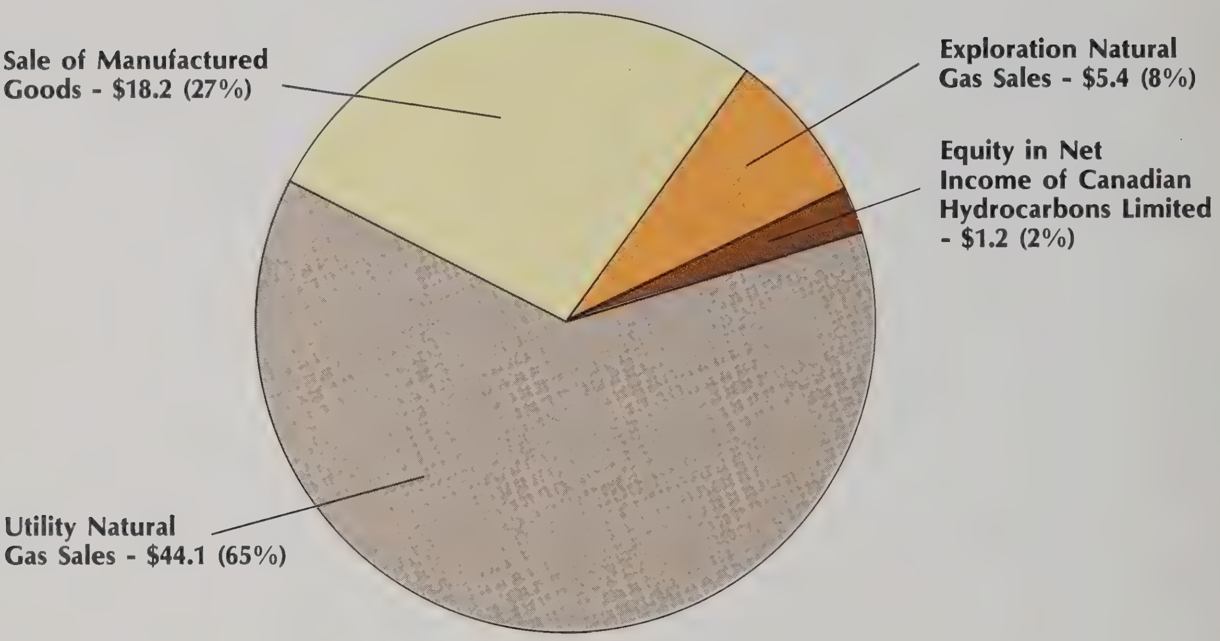


Hilda Area, Alberta
Company 50% Interest (Excluding Medicine Hat Zone)
Company Compressor Station
Company Interest Wells Drilled in 1976
SCALE IN MILES

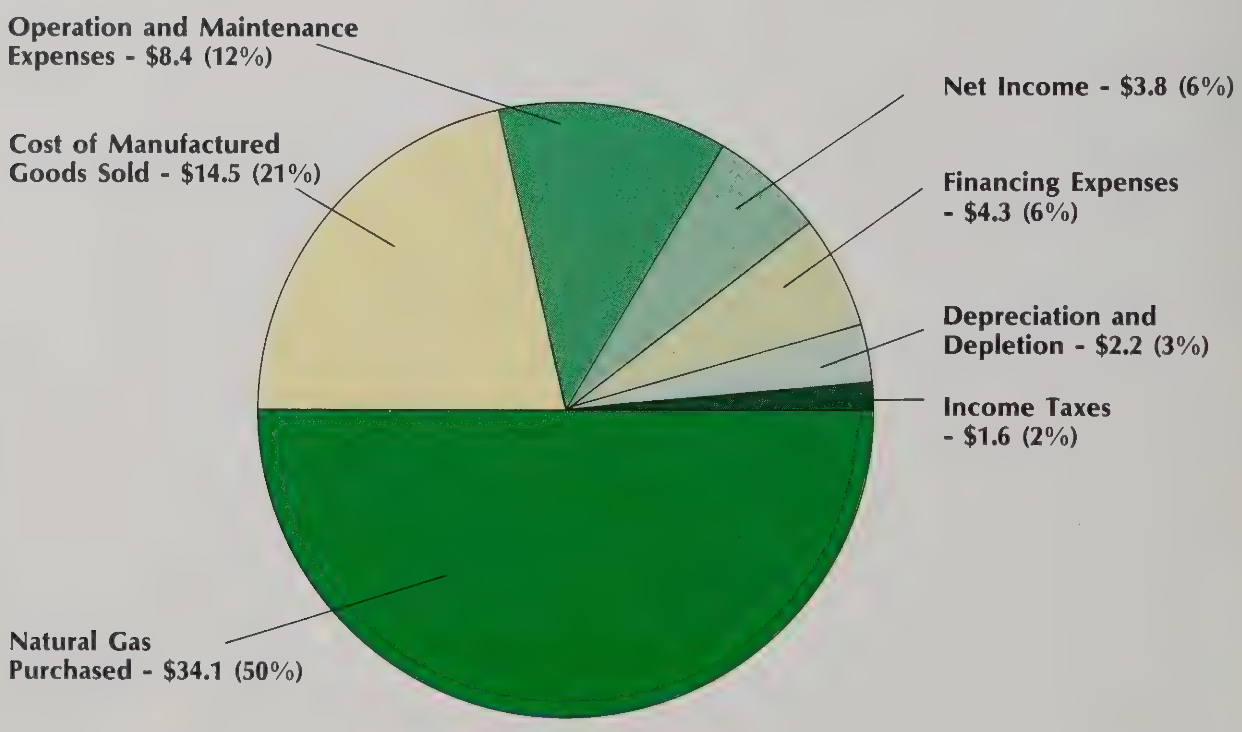

British Columbia
Alberta
Saskatchewan
Prince George
Edmonton
Vancouver
Kelowna
Victoria
Calgary
Medicine Hat
Dauphin
Exploration & Development
Branch Offices (Gas Distribution)
Gas Distribution Systems
Branch Offices (Equipment Distribution)
Manufacturing Plants
Inter-City Gas Transmission Systems
Other Major Gas Pipelines

Quebec
oba
Ontario
Winnipeg
Steinbach
Fort Frances
Thief River
Falls
International Falls
Grand Rapids
Cloquet
Wadena
Minnesota
Toronto
St. Catharines

1976 Sources of Revenue (MILLIONS OF DOLLARS)



1976 Uses of Revenue (MILLIONS OF DOLLARS)



Inter-City Gas Limited

Consolidated Statement of Income

for the years ended December 31, 1976 and 1975

	1976 $	1975 $
Operating Revenue		
Sale of natural gas -		
Utility operations	43,415,006	34,031,662
Exploration operations	5,579,046	2,879,996
Sale of manufactured goods	18,129,171	15,265,991
Other revenue	605,062	452,705
	67,728,285	52,630,354
Operating Expenses		
Natural gas purchased	34,063,721	24,615,009
Cost of manufactured goods sold	14,496,040	11,987,850
Operating and maintenance	7,194,502	5,780,962
Municipal taxes	1,215,013	1,160,556
Depreciation and depletion	2,215,279	1,648,082
	59,184,555	45,192,459
Operating Profit	8,543,730	7,437,895
Financial Expenses		
Interest on long-term debt	3,719,166	2,284,208
Other interest	1,224,315	919,570
Amortization of financing expenses and goodwill	85,230	85,282
Interest capitalized	(699,006)	(647,212)
	4,329,705	2,641,848
Income Before Income Taxes	4,214,025	4,796,047
Income Taxes (note 9)		
Current	904,370	1,146,668
Deferred	1,271,925	1,364,384
Alberta royalty tax credit	(604,120)	(337,084)
	1,572,175	2,173,968
Income before equity in net income of Canadian Hydrocarbons Limited	2,641,850	2,622,079
Equity in net income of Canadian Hydrocarbons Limited	1,207,300	—
Net income for the year	3,849,150	2,622,079
Net income per common share (note 10)	73 cents	56 cents

Inter-City Gas Limited

Consolidated Balance Sheet

as at December 31, 1976 and 1975

ASSETS	1976 $	1975 $
Current Assets		
Cash	1,828,766	1,325,744
Accounts receivable (note 3) -		
Trade and sundry	15,874,555	10,069,634
Conditional sales contracts	75,716	170,421
Income taxes recoverable	185,375	87,766
Inventories (notes 3 and 4)	6,416,751	4,911,386
Prepaid expenses and deposits	317,480	245,530
	24,698,643	16,810,481
Investments - at cost		
Shares of Canadian Hydrocarbons Limited (note 2)	38,783,108	—
Advances to the trustees of employee share purchase plans (note 5)	862,798	735,348
Other	24,699	48,035
	39,670,605	783,383
Fixed Assets (note 6)		
Property, plant and equipment - at cost	60,393,085	52,831,705
Accumulated depreciation and depletion	8,875,210	6,905,905
	51,517,875	45,925,800
Intangible Assets and Deferred Charges — at cost, less amortization		
Financing expenses	944,702	870,584
Natural gas market development	285,784	340,054
Rate hearings and other	758,890	396,043
Goodwill	202,050	222,264
	2,191,426	1,828,945
	118,078,549	65,348,609

Signed on behalf of the board

R G Graham — **Director**

Alan Sweatman — **Director**

LIABILITIES	1976 $	1975 $
Current Liabilities		
Bank advances (note 3)	16,546,749	10,411,405
Accounts payable and accrued liabilities	10,233,536	6,734,944
Income taxes payable	425,347	776,398
Current portion of long-term debt	7,086,535	2,673,591
Customers' security deposits	187,410	187,786
	34,479,577	20,784,124
Customers' Contributions in Aid of Construction	396,950	354,636
Long-Term Debt (note 7)	51,396,351	22,828,934
Deferred Income Taxes (note 9)	4,207,633	2,596,598
	90,480,511	46,564,292

SHAREHOLDERS' EQUITY

Capital Stock (note 8)		
Authorized		
— 600,000 cumulative redeemable first preference shares of the par value of $20 each, issuable in series		
— 262,468 cumulative redeemable second preference shares of the par value of $20 each, issuable in series		
— 10,000,000 common shares		
Issued and fully paid		
— 265,000 8¼% Series B first preference shares	5,300,000	5,300,000
— 200,000 10½% Series C first preference shares	4,000,000	—
— 97,268 6½% Series A second preference shares	1,945,360	1,993,360
— 90,200 7½% Series B second preference shares	1,804,000	1,866,000
— 4,295,795 common shares	6,941,381	3,932,916
	19,990,741	13,092,276
Retained Earnings	7,607,297	5,692,041
	27,598,038	18,784,317
	118,078,549	65,348,609

Inter-City Gas Limited

Consolidated Statement of Changes in Financial Position

for the years ended December 31, 1976 and 1975

	1976 $	1975 $
Source of Funds		
Provided from operations	7,170,742	5,429,367
Proceeds from 10½% Series C first preference shares	4,000,000	—
Proceeds from issue of common shares	3,008,465	127,388
Term bank loans	35,763,172	4,500,000
Customers' contributions in aid of construction	42,314	75,134
Proceeds from sale of fixed assets	—	318,246
Decrease in investments	—	22,752
Proceeds on redemption of preferred shares of Canadian Hydrocarbons Limited	97,500	—
	50,082,193	10,472,887
Use of Funds		
Additions to utility systems and other equipment	748,415	1,727,514
Additions to petroleum and natural gas properties, exploration costs and well equipment	7,166,780	2,756,694
Redemption of long-term debt	12,970,184	3,261,618
Dividends paid to shareholders	1,933,894	1,537,684
Redemption of preference shares	110,000	156,600
Purchase of shares of subsidiary companies	—	254,176
Purchase of shares of Canadian Hydrocarbons Limited	32,287,381	—
Financing expenses and other deferred charges	568,716	131,561
Increase in other investments	104,114	—
	55,889,484	9,825,847
Increase (Decrease) in Working Capital	(5,807,291)	647,040
Working Capital Deficiency - Beginning of Year	3,973,643	4,620,683
Working Capital Deficiency - End of Year	9,780,934	3,973,643
Working capital deficiency is represented by:		
Current liabilities	34,479,577	20,784,124
Current assets	24,698,643	16,810,481
	9,780,934	3,973,643

Inter-City Gas Limited

Consolidated Statement of Retained Earnings

for the years ended December 31, 1976 and 1975

	1976 $	1975 $
Balance - Beginning of Year	5,692,041	4,607,646
Net income for the year	3,849,150	2,622,079
	9,541,191	7,229,725
Dividends paid -		
8¼% Series B first preference shares	437,250	437,241
10½% Series C first preference shares	202,807	—
6½% Series A second preference shares	127,163	132,612
7½% Series B second preference shares	135,750	143,175
Common shares	1,030,924	824,656
	1,933,894	1,537,684
Balance - End of Year	7,607,297	5,692,041

Auditors' Report to the Shareholders

We have examined the consolidated balance sheet of Inter-City Gas Limited as at December 31, 1976 and the consolidated statements of income, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances. For other companies accounted for by the equity method, we have relied on the reports of the auditors who have examined their financial statements.

In our opinion these consolidated financial statements present fairly the financial position of the company as at December 31, 1976 and the results of its operations and the changes in its financial position for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Coopers & Lybrand

CHARTERED ACCOUNTANTS

Winnipeg, Manitoba
March 3, 1977

Notes to Consolidated Financial Statements

For the Year ended December 31, 1976

1. SIGNIFICANT ACCOUNTING POLICIES

Consolidation —

The consolidated financial statements include the assets, liabilities and operating results of all subsidiary companies. The accounts of subsidiary companies are consolidated from the dates of acquisition on the basis of purchase accounting. The amounts by which the purchase price of the subsidiary companies exceeds the fair market value of the assets acquired has been treated as goodwill and is being amortized on a straight line basis over ten years.

Foreign exchange —

The accounts of subsidiaries and divisions operating in the United States are translated into Canadian dollars at the rates of exchange on the balance sheet date for current assets and current liabilities, on the date of the transaction for other balance sheet accounts and at the average rate for the year for revenues and expenses.

Fixed assets —

Natural gas transmission and distribution systems and buildings and equipment are stated at cost which includes interest and overhead amounts capitalized during the construction period. Depreciation is provided on the straight line method with rates varying between 1.7% and 30.0% based on the estimated useful life of those assets.

Petroleum and natural gas properties, exploration costs and well and gathering systems are accounted for on the full cost method of accounting, whereby all costs, including interest and overhead, of exploring for and developing petroleum and natural gas properties are capitalized. These costs are depleted by the unit of production method based on estimated recoverable reserves.

Deferred charges —

Amortization of financing expenses and other deferred charges is provided on the straight line method over periods of five to twenty years.

Income taxes —

Regulatory agencies have directed certain subsidiary companies to provide only those income taxes currently payable in its financial statements and in calculating its rate of return for rate making purposes. However, for all other operating divisions, the company, in accordance with the recommendations of the Canadian Institute of Chartered Accountants, provides for deferred income taxes on all timing differences between accounting income and taxable income, including those relating to exploration, development and acquisition of petroleum and natural gas properties.

Inventories —

Inventories are stated at the lower of cost or net realizable value. Cost is determined for work in progress and finished goods at standard prices and for raw materials and supplies on a first-in, first-out basis.

2. INVESTMENT IN CANADIAN HYDROCARBONS LIMITED

In August 1976, the company acquired 2,550,256 common shares of Canadian Hydrocarbons Limited representing 49.7% of its outstanding common shares. In addition, the company acquired preference shares of Canadian Hydrocarbons Limited, with a par value of $5,915,000. This acquisition was achieved through acquiring for $33,843,412 cash all the outstanding shares of Elwill Development Limited. The company subsequently acquired an additional 6,400 common shares of Canadian Hydrocarbons Limited, increasing its interest to 49.8%.

The company is following the equity method of accounting for its interests in Canadian Hydrocarbons Limited. As at December 31, 1976, the company's investment is composed of:

	$
Common stock at equity	32,965,608
Preferred shares at cost	5,817,500
	38,783,108

3. SECURITY FOR BANK ADVANCES AND TERM LOANS

Current and term bank loans are generally secured by a pledge of inventories, accounts receivable, production proceeds, shares of certain companies and interests in certain petroleum and natural gas properties. In addition, a demand debenture in the amount of $3,500,000 securing a floating charge on the non-utility subsidiary companies' assets has been given as collateral security.

4. INVENTORIES

Inventories are classified as follows:

	1976	1975
	$	$
Raw materials	1,161,794	1,087,320
Work in process	486,193	386,754
Finished goods	3,995,366	2,728,303
Materials and supplies	773,398	709,009
	6,416,751	4,911,386

5. EMPLOYEE SHARE PURCHASE PLANS

Pursuant to the rights offered to common shareholders (see note 8 (a)) 43,838 common shares were purchased by the trustees of the plans during the year (no purchases in 1975). An amount of $24,775 was repaid during the year by the trustees to the company and the balance due from the trustees at December 31, 1976 amounted to $862,798 (1975 - $735,348).

6. FIXED ASSETS

Property, plant and equipment are classified as follows:

	Cost	Accumulated depreciation and depletion	1976	1975
	$	$	$	$
Utility transmission and distribution systems	35,141,287	5,683,932	29,457,355	29,677,923
Petroleum and natural gas properties and exploration costs	14,983,113	1,461,049	13,522,064	10,031,145
Well equipment and gathering systems	8,539,763	1,029,290	7,510,473	5,404,778
Land and buildings	663,049	178,219	484,830	405,251
Machinery, equipment and furniture	1,065,873	522,720	543,153	406,703
	60,393,085	8,875,210	51,517,875	45,925,800

7. LONG-TERM DEBT

The details of long-term debt of the company and its subsidiary companies are as follows:

	1976		1975	
	Current	Long-term	Current	Long-term
	$	$	$	$
Inter-City Gas Limited				
Term bank loans bearing interest at 1% to 3% above bank prime rate, due 1980 and 1981 (U.S. $5,310,000)	766,840	4,455,475	60,000	485,000
7% debentures - Series B maturing 1982	79,500	825,000	62,200	925,000

	1976		1975	
	Current $	Long-term $	Current $	Long-term $
8% first mortgage bonds - Series A maturing 1989 (U.S. $3,400,000)	151,350	3,503,012	168,246	3,637,200
9½% first mortgage bonds - Series B maturing 1994 (U.S. $1,800,000)	100,900	1,644,920	96,760	1,741,680
9½% first mortgage bonds - Series C maturing 1994	50,000	850,000	50,000	900,000
Inter-City Gas Utilities Ltd.				
6% first mortgage bonds - Series A maturing 1977	37,500	—	37,500	37,500
6% first mortgage bonds - Series B maturing 1982	25,000	225,000	25,000	250,000
6% first mortgage bonds - Series C maturing 1985	57,000	1,530,000	57,000	1,587,000
7% debentures - Series A maturing 1979	25,500	287,500	—	341,500
Inter-City Pipelines Ltd.				
Term bank loan bearing interest at 1% above bank prime rate, due 1980 and 1983	770,000	4,720,000	370,000	1,490,000
Inter-City Minnesota Pipelines Ltd. - and ICG Transmission Limited				
9½% joint and several promissory note due 1991, secured by 8% joint and several first mortgage bonds maturing 1991 (U.S. $3,970,000)	267,385	3,754,956	268,572	4,023,528
Minell Pipeline Ltd.				
Term bank loan bearing interest at 3% above bank prime rate, due 1980 (U.S. $571,667)	70,630	501,666	70,000	571,666
Inter-City Manufacturing Ltd.				
Term bank loans bearing interest at 1% to 1¼% above bank prime rate, due 1980 and 1983	1,890,000	22,780,000	1,140,000	4,670,000
Term bank loans bearing interest at 0.37% to 1¼% above bank prime rate, due 1978 and 1980 (U.S. $9,182,500)	2,794,930	6,318,822	268,313	2,168,860
	7,086,535	51,396,351	2,673,591	22,828,934

Under the provisions of the various indentures and agreements the companies are required to make the following sinking fund installments and term bank loan repayments during the next five years:

Year	$
1977	7,086,535
1978	9,086,482
1979	5,245,622
1980	8,321,658
1981	6,621,138

8. CAPITAL STOCK

(a) In April 1976, the company offered to its common shareholders, rights to purchase one additional share for each four presently held at a price of $3.50 per share. As a result of this offer, 859,067 common shares were issued for a consideration of $3,006,735.

(b) In July 1976, the company issued 200,000, 10½% first preference shares, Series C at a price of $20.00 per share, for a total consideration of $4,000,000.

(c) The company has reserved 599,340 common shares on the exercise of share purchase warrants at $3.50 per share up to July 31, 1981. During the year 560 warrants were exercised for a consideration of $1,730.

(d) The company is required by its letters patent to purchase annually in the market, within certain limits, a minimum of 3% of the outstanding 6½% Series A second preference shares of which 2,400 were purchased and cancelled during 1976 and a minimum of 3% of the outstanding 7½% Series B second preference shares of which 3,100 were purchased and cancelled in 1976. Effective May 1977 the company is required to purchase annually a minimum of 7% of the outstanding 8¼% Series B first preference shares. Purchase fund commitments on the 10½% Series C first preference shares commence in 1977 at 7% of the original issue amount for each of the first five years, at 13% for each of the next five years and at 5% for each year thereafter.

9. DEFERRED INCOME TAXES

As explained in the note on accounting policies, the company does not follow the tax allocation basis for its gas utility and pipeline operations. If tax allocation had been followed in respect of all timing differences between accounting income and taxable income, the provision for deferred income taxes would have increased and consolidated net income would have decreased by $59,800 (1975 - ($700)). At December 31, 1976 the accumulated deferred income taxes would have amounted to approximately $2,957,400 (1975 - $2,897,600), in addition to the amounts recorded in the accounts.

10. NET INCOME PER COMMON SHARE

The net income per common share is calculated on the weighted average number of shares outstanding during the respective years. For the purpose of calculating the dilution, if any, per common share it has been assumed that the share warrants for 599,340 common shares were exercised on January 1, 1976 and the proceeds received therefrom earned a rate of return equivalent to that earned on the book value of the common shareholders' equity in 1976. Based on this assumption there is no dilution of the 1976 net income per common share. The amount of imputed income was $421,636.

11. SUPPLEMENTARY INFORMATION

	1976 $	1975 $
(a) Included in other revenue are the following amounts —		
Income from investments	186,237	17,175
Discount on shares and debentures purchased for cancellation	34,709	62,341
(b) Included in operating and maintenance expense are the following amounts for the amortization of deferred charges —		
Natural gas market development	52,603	46,435
Rate hearings and other	61,898	35,798
(c) The aggregate remuneration paid to directors and senior officers of the company in their capacity as director, officer or employee	426,950	357,700

12. ANTI-INFLATION ACT

The company is subject to the restraint of dividends under the terms of the Anti-Inflation Act and Regulations which became effective October 14, 1975.

Under the legislation the amount of dividends which the company can declare or pay during the period from October 14, 1976 to October 13, 1977 will be limited to 26 cents per common share. Of this amount, 12 cents per common share was paid to shareholders on December 15, 1976.

Inter-City Gas Limited

Ten Year Summary of Operations

(THOUSANDS OF DOLLARS)

	1976	1975	1974	1973
Operating Revenue				
Sale of Natural Gas				
Exploration Operations	$ 5,579	2,880	177	—
Utility Operations	43,415	34,031	22,372	18,324
Sale of Manufactured Goods	18,129	15,266	14,292	14,018
Other Income	605	453	498	347
Total	67,728	52,630	37,339	32,689
Operating Expenses				
Natural Gas Purchased	34,064	24,615	14,307	11,467
Cost of Manufactured Goods Sold	14,496	11,988	10,694	11,118
Operating & Maintenance	7,194	5,781	4,468	3,887
Municipal Taxes	1,215	1,160	916	826
Depreciation & Depletion	2,215	1,648	919	797
Total	59,184	45,192	31,304	28,095
Operating Profit	8,544	7,438	6,035	4,594
Financial Expenses				
Interest on Funded Debt	3,719	2,284	2,176	1,725
Other Interest	1,225	920	839	607
Amortization of Financing Expenses	85	85	54	59
Interest Capitalized	(699)	(647)	(820)	(255)
Minority Interest	—	—	6	3
	4,330	2,642	2,255	2,139
Income Before Income Taxes	4,214	4,796	3,780	2,455
Income Taxes	1,572	2,174	1,659	1,003
Income Before Equity in Income of Canadian Hydrocarbons Limited	2,642	2,622	2,121	1,452
Equity in Income of Canadian Hydrocarbons Limited	1,207	—	—	—
Net Income of the year	$ 3,849	2,622	2,121	1,452
Dividends Paid				
Preferred Shares	$ 903	713	537	352
Common Shares	1,031	825	683	378
Earnings Per Common Share	$ .73	$ .56	$ .45	$ .37
Fixed Assets				
Utility & Pipelines	$35,368	35,116	33,991	32,274
Manufacturing	1,333	1,127	998	935
Oil & Gas Properties	23,692	16,589	13,906	6,079
Total	$60,393	52,832	48,895	39,288
Utility Natural Gas Sales (Millions of Cubic Feet)	27,951	27,734	30,019	27,579
Utility Customers at year-end	29,781	28,699	27,376	25,451

1972	1971	1970	1969	1968	1967
—	—	—	—	—	—
17,880	15,380	10,323	8,134	7,547	6,459
9,132	6,762	2,949	2,500	—	—
183	117	131	94	159	95
27,195	22,259	13,403	10,728	7,706	6,554
11,491	10,234	6,685	5,104	4,903	4,010
7,488	5,708	2,541	2,013	—	—
3,098	2,378	1,475	1,321	848	812
756	628	509	492	453	376
668	568	410	371	330	292
23,501	19,516	11,620	9,301	6,534	5,490
3,694	2,743	1,783	1,427	1,172	1,064
1,023	1,174	610	435	369	361
635	341	214	295	303	229
55	28	28	23	31	33
(120)	(42)	(9)	(14)	(17)	(19)
11	22	—	30	1	2
1,604	1,523	843	769	687	606
2,090	1,220	940	658	485	458
547	254	264	99	11	10
1,543	966	676	559	474	448
—	—	—	—	—	—
1,543	966	676	559	474	448
362	292	221	226	230	230
248	198	158	124	119	119
$ .43	$ .26	$ .18	$ .13	$ .10	$ .09
30,267	28,934	25,607	17,369	15,296	15,125
877	555	496	471	—	—
4,082	624	—	—	—	—
35,226	30,113	26,103	17,840	15,296	15,125
29,680	25,904	16,387	12,869	13,299	10,665
23,986	22,644	20,629	19,941	18,126	17,297

Inter-City Gas Limited

DIRECTORS

C. ROY BEENHAM
Winnipeg, Manitoba
Senior Vice-President
Inter-City Gas Limited

G.R. CHATER
Toronto, Ontario
President, Grafton Group Limited

H.E. DYNES
Toronto, Ontario
President and Chief Executive Officer
Traders Group Limited

ROBERT G. GRAHAM
Winnipeg, Manitoba
President and Chief Executive Officer
Inter-City Gas Limited

WAYNE R. HARDING
Winnipeg, Manitoba
Executive Vice-President
Inter-City Gas Limited

JAMES W. McCUTCHEON, Q.C.
Toronto, Ontario
Partner
Shibley, Righton & McCutcheon

GORDON P. OSLER
Toronto, Ontario
Vice-Chairman of the Board
British Steel Corporation (Canada) Ltd.
and Chairman of the Board
Slater Steel Industries Ltd.

E.P. RIMMER
Winnipeg, Manitoba
Vice-President
Inter-City Gas Limited

ALAN SWEATMAN, Q.C.
Winnipeg, Manitoba
Partner
Thompson, Dorfman, Sweatman

OFFICERS

ROBERT G. GRAHAM
President and Chief Executive Officer

WAYNE R. HARDING, C.A.
Executive Vice-President

C. ROY BEENHAM
Senior Vice-President

E.P. RIMMER, P. ENG.
Vice-President

G.H. LUCAS
Vice-President

R.J. DAHNKE, P. ENG.
Vice-President

B.W. HALL
Secretary

ROBERT W. DUNBAR, C.A.
Controller

SOLICITORS

THOMPSON, DORFMAN, SWEATMAN

AUDITORS

COOPERS & LYBRAND

TRANSFER AGENTS AND REGISTRAR

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